

IRS



Fact Sheet

Media Relations Office

Washington, D.C.

Media Contact: 202.622.4000

www.IRS.gov/newsroom

Public Contact: 800.829.1040

Home Office Deduction Reminders

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WASHINGTON— Overstated adjustments, deductions, exemptions and credits account for up to \$30 billion per year in unpaid taxes, according to IRS estimates.

In order to educate taxpayers regarding their filing obligations, this fact sheet, the fourth in a series, explains the rules for deducting home office expenses.

Home Office Deduction: Basic Requirements

Generally, expenses related to the rent, purchase, maintenance and repair of a personal residence may not be deducted as a business expense. However, taxpayers who use a portion of their home for business purposes may be able to take a home office deduction if they meet certain requirements. Expenses that may be deducted include the business portion of real estate taxes, mortgage interest, rent, utilities, insurance, painting, repairs and depreciation. Note: The amount of depreciation deducted, or that could have been deducted, decreases the basis of your property.

In order to claim a deduction for that part of a home used for business, taxpayers must use that part of the home:

- Exclusively and regularly as their principal place of business, as a place to meet or deal with patients, clients or customers in the normal course of their business, or in connection with their trade or business where there is a separate structure not attached to the home; or
- On a regular basis for certain storage use such as inventory or product samples, as rental property, or as a home daycare facility.

In addition, taxpayers working as employees can claim this deduction only if the regular and exclusive business use of the home is for the convenience of their employer and the portion of the home is not rented by the employer.

“Exclusive use” means a specific area of the home is used only for trade or business. “Regular use” means the area is used regularly for trade or business. Incidental or occasional business use is not regular use.

Non-business profit-seeking endeavors such as investment activities do not qualify for a home office deduction, nor do not-for-profit activities such as hobbies.

Example: An attorney uses the den in his home to write legal briefs or prepare clients' tax returns. The family also uses the den for recreation. The den is not used exclusively in the attorney's profession, so a business deduction cannot be claimed for its use.

These requirements are discussed in greater detail in Publication 587, Business Use of Your Home.

Computing the Amount of Home Office Deduction

Generally, the amount of the deduction depends on the percentage of the home that is used for business. The deduction will be limited if gross income from the business is less than the total business expenses.

A taxpayer can use any reasonable method to compute business percentage, but the most common methods are to:

- Divide the area of the home used for business by the total area of the home, or
- Divide the number of rooms used for business by the total number of rooms in the home if all rooms in the home are about the same size.

Taxpayers may not deduct expenses for any portion of the year during which there was no business use of the home. If the gross income from business use of the home is less than the total business expenses, the deduction for certain expenses is limited.

Publication 587 includes examples, worksheets and additional information on computing the allowable deduction.

Personal Expenses Are Not Business Expenses

It is important for taxpayers to realize that business expenses may be deducted only if they are ordinary and necessary for the particular type of business. Personal, family and living expenses are not deductible under any circumstances. A common error is to deduct expenses for a portion of the home that is not used regularly and exclusively for business.

Example: The basic local telephone service charge, including taxes, for the first telephone line into a home is a nondeductible personal expense. However, charges for business long-distance phone calls on that line, as well as the cost of a second line into a home used exclusively for business, are deductible business expenses.

The IRS encourages taxpayers to familiarize themselves with the requirements before taking a home office deduction and to keep complete and accurate records to substantiate deductions. According to IRS research, understated business income, including underreported receipts and overstated expenses, is an area where compliance is a concern. In addition to increasing outreach and education in these

areas, the IRS will also be focusing enforcement efforts, including examinations, on these issues.